



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

**DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224**

Release Number: **201149043**  
Release Date: 12/9/2011  
Date: September 15, 2011

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:  
Form 1120

Tax Years:  
2007, 2008, 2009

UIL: 501.04-00

Dear

This is our final determination that you do not qualify for exemption from Federal income tax under Internal Revenue Code section 501(a) as an organization described in Code section 501(c)(4).

We made this determination for the following reason(s):

You are not operated exclusively for the promotion of social welfare as described in section 501(c)(4) of the Code. Your primary activity is providing managerial services in exchange for fees under the terms of a management contract. Moreover, your activities serve private rather than public interests.

You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at

1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Elizabeth Kastenbergr for

Lois Lerner  
Director, Exempt Organizations

Enclosure  
Notice 437  
Redacted Proposed Adverse Determination Letter  
Redacted Final Adverse Determination Letter



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

Date: March 26, 2010

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

B =  
C =  
D =  
E =  
F =  
G =  
M =  
Date =  
State =  
Year 1 =  
Year 2 =  
Year 3 =  
Commission =

Dear

We have considered your application for recognition of exemption from Federal income tax under Internal Revenue Code section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code section 501(c)(4). The basis for our conclusion is set forth below.

Facts:

You are a nonstock corporation incorporated on Date in State. Your Articles of Incorporation state that you were formed to:

...engage in activities which promote the efficient operation of M in the ports of E and E, facilitate the efficient movement of international cargo through the E metropolitan area, ease truck traffic congestion on the highways in and around the ports, and improve the environment and safety of the surrounding communities,

through the facilitation, implementation and support of a program to promote operation of M in off-peak hours including through the collection and distribution of funds to promote such non-peak hour operations of M facilities and through the implementation of a D program, and any other activities relative to those purposes that are appropriate and proper.

You state that the for-profit, privately held M operators (members), who compete for business at ports E and F, created you to solve problems in the port community. Previously, the members operated primarily during weekday business hours (peak hours) and only at low levels at night and on weekends (off-peak hours). Their limited operating schedules created increasing traffic congestion, air pollution and security risk problems in the port communities. Shipping companies began diverting ships to other ports and building additional delivery days into their supply chains. You state that the members were reluctant to relieve the problem by increasing off-peak hour operations because the additional costs would place them at a competitive disadvantage.

Under pressure from the public and from proposed legislation, and with the approval of the Commission, which regulates certain M activities, the members created B, C, and you to promote M during off-peak hours by assessing and collecting fees on cargo moved during peak hours. You state that by assessing a fee during the peak hours, members have an incentive to use M during off-peak hours when the fee is not assessed. All members are obligated to operate during off-peak hours and to absorb associated costs.

The members hold common control of B, C, and you. Your application states that B is a limited liability company (LLC). The M operators are the members of B and B has no direct employees. C is an agreement between the M operators that obligates them to operate during off-peak hours and absorb off-peak hour costs in accordance with a set schedule.

Your primary activity is providing managerial services to B in exchange for management fees. The management agreement provides that your role is to collect fees imposed on goods that move through M during peak hours and to distribute such fees to the members of B. Each month, you distribute the proceeds, net of refunds, your management fees, operating costs and an operating reserve, to B, who in turn distributes the net proceeds to the M operator members in amounts that are proportionate to the percentage of total cargo that they moved through the terminals. Your application states that your sole source of revenue is the management fees you receive pursuant to the management agreement.

Your Articles of Incorporation provide that your members must be members of C. Your Board of Directors is composed of six directors. Annually, each of the five largest members (based on highest percentage of total cargo moved through M), will appoint representatives to your board. The sixth director is elected by a majority vote of the members and may not be employed by one of the five largest members or an affiliate of any such member. In addition, the sixth director must be nominated by a member other than one of the five largest. Each director is entitled to a single, equally weighted vote. Each member votes in proportion to the percentage of total cargo moved by such member through M during the calendar year.

You state that you have also installed and operate the D program which is a system designed to automate the identification and authorization of the trucks that serve the terminals. You acquired the system from a commercial company that distributes the identification tags and interfaces its database with the terminals' operating systems and replace any lost or damaged units. The security checkpoints use the electronic system to identify the trucks moving through the port. The D program helps your members stay in compliance with federal regulations that require them to ensure the safety of the ports by inspecting the cargo trucks that pass through the ports.

You assert that you lessen the burdens of government by engaging in a charitable activity. You provided information that the State legislature proposed a bill in Year 1 and again in Year 2, which included the following provisions:

1. Create an entity of local government that will establish an infrastructure fund and finance port or harbor infrastructure improvements.
2. Establish a governing authority including representatives from the ports, city councils, workers and other members of the port community.
3. State that the provisions of the bill would not become operative if a local agency or authority has established a fee on container cargo moving through the ports and at least 20 percent of inbound cargo is transported during off-peak hours.
4. Deposit all revenues in a fund for expenditures to encourage other means of shipping cargo, to repair the transportation infrastructure, and encourage off-peak hour shipping.
5. Require all of the marine terminals at ports E and F to provide off-peak operations.

You state that the prospective legislation from Year 2 specifically referred to you in the provisions. In Year 3, public information shows that the bill was vetoed by the governor of State. To date, no other legislation with similar provisions is pending.

#### Law:

Section 501(c)(4) of the Internal Revenue Code (Code) provides an exemption from federal tax for civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare.

Section 1.501(c)(4)-1(a)(1) of the Income Tax Regulations (regulations) states that, in general, an organization may be exempt as an organization described in section 501(c)(4) if it is not organized or operated for profit and it is operated exclusively for the promotion of social welfare.

Section 1.501(c)(4)-1(a)(2) of the regulations states that, in general, an organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community. An organization embraced within this section is one that is operated primarily to bring about civic betterments and social improvements. A "social welfare" organization will qualify for exemption as a charitable organization if it falls within the definition of "charitable" set forth in paragraph (d)(2) of section 1.501(c)(3)-1.

Section 1.501(c)(3)-1(d)(2) of the regulations states that the term "charitable" is used in section 501(c)(3) in its generally accepted legal sense. Such term includes lessening the burdens of Government.

Rev. Rul. 54-394, 1954-2 C.B. 131 holds that an organization whose sole activity was to provide television reception for its members on a cooperative basis in an area not readily adaptable to ordinary reception is not exempt under section 501(c)(4) of the Code. Members were required to contract for and to pay service and installation fees. In its conclusion that the organization did not qualify for exemption, this ruling stated:

When an organization's only activity is to provide television reception on a cooperative basis to its members, who contract and pay for such services, such organization is held to operate for the benefit of its members rather than for the promotion of the welfare of mankind.

Rev. Rul. 62-167, 1962-2 C.B. 142 holds that an organization that is organized to construct and maintain a translator, or reflector-type television station, capable of receiving signals of television stations and reproducing such signals so that satisfactory television may be available to the community in general is a social welfare activity. The organization made membership available to all persons in the area. It derived its income from membership fees and donations. It disbursed funds for the maintenance and operation of the television relay station.

Rev. Rul. 69-385, 1969-2 C.B. 123 holds that a community welfare corporation that purchases and sells unimproved land and engages in other business activities, the profits from which are distributed to members, is not exempt under section 501(c)(4) of the Code.

Rev. Rul. 75-199, 1975-1 C.B. 160 holds that an organization that provides sick benefits for its members and paid death benefits to the beneficiaries of members does not qualify as an exempt organization under section 501(c)(4) of the Code. Membership in the organization was restricted to individuals of good moral character and health who belonged to a particular ethnic group and resided in a stated geographic area. The organization's activities consisted of holding monthly meetings and maintaining an established system for the payment of sick and death benefits. It derived its income primarily from membership dues and used that income to pay benefits to members and miscellaneous operating expenses. In concluding that this organization did not qualify for exemption under section 501(c)(4), this revenue ruling found that it was essentially a mutual, self-interest organization. It used its income to provide direct and economic benefits to members and any benefit to the larger community was minor and incidental. The ruling states:

Where the benefit from an organization is limited to that organization's members (except for some minor and incidental benefit to the community as a whole), the organization is not operated exclusively for the promotion of social welfare within the meaning of section 501(c)(4) of the Code.

Rev. Rul. 79-316, 1979-2 C.B. 228, holds that an organization whose purpose is to prevent liquid spills within a city port area and to develop a program for the containment and cleanup of liquid spills that do occur is entitled to exemption as a social welfare

organization under section 501(c)(4) of the Code provided that its services are equally available to members and nonmembers and both members and nonmembers are charged on the same basis for the cleanup services rendered.

Rev. Rul. 85-1, 1985-1 C.B. 178, sets out a two-part test for determining whether an organization's activities lessen the burdens of government. First, it is necessary to determine whether the governmental unit considers the organization's activities to be its burden. The second part of the test is whether these activities actually lessen the burdens of the government. An activity is a burden of government if there is an objective manifestation by the governmental unit that it considers the activities of the organization to be its burden. Whether the organization is actually lessening the burdens of government is determined by considering all relevant facts and circumstances.

Rev. Rul. 85-2, 1985-1 C.B. 178, held that an organization that provides legal assistance to guardians ad litem who represent abused and neglected children before a juvenile court that requires their appointment lessens the burdens of government, and, therefore, qualifies for exemption under section 501(c)(3) of the Code. The determination of whether an organization's activities actually lessen the burdens of government is based on all the relevant facts and circumstances.

Contracting Plumbers Cooperative Restoration Corp. v. United States, 488 F.2d 684 (2d Cir. 1973), cert. denied, 419 U.S. 827 (1974), held that a private, nonprofit cooperative, which was organized by plumbers to insure efficient repair of "cuts" made in city streets in the course of members' plumbing activities, with each member enjoying such economic benefits precisely to the extent that he used and paid for restoration services, was not exempt from federal income taxation as a civic organization or a business league. Previously the "cuts" were repaired by the city and the plumber was billed for the work. The court found that while all the plumbers received some incidental benefit from the goodwill created by the properly filled excavations, each individual member received more in economic terms precisely to the extent that he used the restoration service. "[W]here, as here, ... individual benefits are precisely proportional to the member's financial involvement in the organization, the fundamentally non-exempt purpose of providing a necessary service at reduced cost becomes too clear to be ignored."

#### Analysis:

Based on the information you submitted, we conclude that you are not operated for the exempt purpose described in section 501(c)(4) of the Code. An organization is recognized as exempt under section 501(c)(4) only if it can establish that it is not organized for profit and operates primarily for the promotion of social welfare. An organization does not operate exclusively for the promotion of social welfare if it serves private rather than public interests. See sections 1.501(c)(4)-1(a)(1) and (2) of the regulations. More specifically, an organization that primarily operates to provide its members with direct benefits in consideration for payments from the members is a mutual benefit society that does not qualify under section 501(c)(4) as a social welfare organization.

The information you provided indicates that your members organized you for a business purpose and limited membership to M operators that signed the agreement. Your members



receive services and net proceeds in proportion to the extent they use your services. Like the organization in Contracting Plumbers Cooperative Restoration Corp. v. United States, 488 F.2d 684 (2d Cir. 1973), cert. denied, 419 U.S. 827 (1974), your members created you in response to community and legislative pressure, which gave your members a substantial business interest. Unlike the proposed state legislation, which would establish a governing authority composed of representatives from the ports, the city councils, the city and county transportation authorities, and other local government representatives, your thirteen for-profit members hold complete control of B, C, and you. It is clear that your for-profit members organized you for a business purpose, to get services at a low cost.

Officers and directors that receive benefits from the activities of a social welfare organization are not regarded as receiving private benefit or inurement if all of the insiders benefit in the same way and to the same extent as other members of the community. However, unlike the organization described in Rev. Rul. 79-316, 1979-2 C.B. 228, your services are not equally available to your members and are not available to nonmembers as well as members. Like the organization described in Contracting Plumbers Cooperative Restoration Corp. v. United States, 488 F.2d 684 (2d Cir. 1973), cert. denied, 419 U.S. 827 (1974), your members enjoy the economic benefits of your activities precisely to the extent that they use your services. The members who move the highest percentage of total cargo through M each month sit on your board and get the highest percentage of the vote and the largest distribution of net earnings. Your members receive private benefits from your activities in direct proportion to the extent they use your services. Accordingly, you provide private benefits to your members.

Organizations will not qualify under section 501(c)(4) if they operate primarily for the benefit of their members, rather than for benefiting the community as a whole. Two rulings distinguish mutual benefit societies from social welfare organizations; Rev. Rul. 54-394, 1954-2 C.B. 131 held that an organization that provided television distribution, service, maintenance and repair services for fees was not entitled to exemption. Since the organization only provided services to its members and placed restrictions on membership, it was a mutual benefit organization. See also Rev. Rul. 75-199, 1975-1 C.B. 160. Compare to Rev. Rul. 62-167, 1962-2 C.B. 142, which held that an organization created to make television available to all television owners in the community was entitled to exemption. Since membership was available to all and the organization obtained members and contributions on a voluntary basis, it was a social welfare organization. See also Rev. Rul. 79-316, 1979-2 C.B. 228. When an organization limits the benefits it provides to its members, it is not operated exclusively for the promotion of social welfare within the meaning of section 501(c)(4) of the Code.

An applicant for exempt status under section 501(c)(4) must first show that it is operated exclusively to promote the common good and general welfare of the people of the community. While your activities may provide some incidental public benefit, we do not agree that you operate primarily for social welfare purposes under section 501(c)(4). An organization is not operated for the promotion of social welfare if its primary activity is carrying on a business with the general public in a manner similar to organizations operated for-profit. Unlike the proposed state legislation, you have not indicated that you will use excess funds to improve the common good and general welfare of the port community by financing port or harbor infrastructure improvements, undertaking projects to improve the flow and efficiency of container cargo to and from the ports, or mitigating the air pollution caused by the movement of container cargo to and



from the ports. You are essentially a mutual, self-interest type of organization. The management services you perform for your members provide an economy or convenience relating to the operation of M. See Rev. Rul. 69-385. You also operate the D program to help your members stay in compliance with federal regulations. Therefore, you operate primarily for the benefit of your for-profit members and you do not operate exclusively to promote the common good and general welfare of the port community. These facts show that you operate primarily for the benefit of your members instead of promoting the general welfare of the community. Accordingly, you do not qualify under section 501(c)(4) as a social welfare organization.

An organization that has first established that it meets the basic requirements of section 501(c)(4) and operates exclusively for the common good and general welfare of the community may show that it also furthers a charitable purpose. Section 1.501(c)(3)-1(d)(2) of the regulations. You have asserted that you promote social welfare as a charitable purpose by conducting activities that lessen the burdens of government. The determination of whether an organization actually lessens the burdens of government requires a two-part analysis of the relevant facts and circumstances.

Rev. Rul. 85-1, 1985-1 C.B. 178, explains that the first part of the two-part test in the determination of whether an activity lessens the burdens of government is whether the local governmental unit considers the organization's activities to be its burden. The fact that the government or an official of the government expresses approval of an organization and its activities is not sufficient to establish that an organization is lessening the burdens of government. An objective manifestation by the government that it considers an activity to be part of its burden may indicate that the activity is a burden of government. Factors that provide evidence that a local government considers an activity to be its burden include, but are not limited to, the following:

1. The interrelationship between the governmental unit and the organization,
2. The degree of control the local government has over the activities, and
3. The funding of an organization's activities by the government.

Rev. Ruls. 85-1 and 85-2, 1985-1 C.B. 178, explains that the second test requires that the organization conducting the activity demonstrate that its activities actually lessen the burdens of government. When an organization seeks to show that its activities lessen a burden of government on the basis that a state statute authorizes the activities it performs, the statute must be read in its entirety to ascertain whether the legislative body intended the activities to be performed on a normal commercial basis or by a nonprofit organization. If the statute, read as a whole, indicates that the legislative body intended that the private sector perform the activities, those activities do not lessen the burdens of government.

Based on the facts and circumstances provided, you have not demonstrated conclusively that a governmental unit considers your activities to be part of its burden or that your activities actually lessen the burdens. You submitted copies of articles and letters from government officials that expressed appreciation and overall approval of B's off-peak hour program. However, your records show that representatives from the port communities and local city councils are not involved in your day-to-day management activities. Your for-profit members hold complete

control of your board. In addition, your primary source of revenue is membership fees, not support from the local government.

The proposed legislation would have established a community-based governing authority that requires the ports to assess and collect user fees that will fund projects to improve the port community through the issuance of revenue bonds. One provision stated that the ports might contract with you to collect the user fee. The relationship between you and the local government is more in the nature of a commercial contract for services. Since, read as a whole, the proposed legislation shows that state lawmakers intended the ports to satisfy their burden by contracting, on a commercial basis, for services, you do not lessen the government's burden.

Since you have not satisfied the first and second parts of the two-part test set out in Rev. Ruls. 85-1 and 85-2, your primary activities do not meet the definition of "charitable" set forth in the regulations.

Finally, section 501(c)(4) provides tax exemption to organizations that engage in "social welfare". Section 501(c)(4) of the Code and section 1.501(c)(4)-1(a) of the regulations specifically state that an organization that is not organized for profit but operated exclusively for the promotion of social welfare and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes shall be exempt from tax. All organizations applying for exemption as a social welfare organization must meet the specific requirements of section 501(c)(4) to be exempt under that section. Section 1.501(c)(4)-1(a)(2)(ii) of the regulations states that a social welfare organization that is not exempt from taxation as an organization described in section 501(c)(3) may qualify under section 501(c)(4) even though it is an "action" organization, but it must otherwise qualify under this section. The reverse is not true. An organization that fails to qualify for exempt status under section 501(c)(4) will not qualify under section 501(c)(3). To sum, the statute, regulations and published guidance have one common element, that an organization must meet the requirements of section 501(c)(4) to be exempt under that subsection. You are not involved in social welfare activities within the meaning of section 501(c)(4) and therefore not exempt under that section.

#### Conclusion:

Based on the information provided, you have not shown that you are organized and operate exclusively for the promotion of social welfare. Your activities demonstrate that your primary activity is to provide services for your members, rather than to provide a benefit to the community as a whole. Your activities further the business interests of your members; they do not lessen the burden of government or otherwise further charitable purposes. Since you do not operate primarily to promote the common good and general welfare of the port community, you are not operated exclusively for the promotion of social welfare as described in section 501(c)(4) of the Code.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

*Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.*

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at [www.irs.gov](http://www.irs.gov), Forms and Publications.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to this address:

Internal Revenue Service  
TE/GE

1111 Constitution Ave, N.W.  
Washington, DC 20224

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Robert Choi  
Director, Exempt Organizations  
Rulings & Agreements
